

General Information Letter: Payments of employee benefits that are not subject to federal income tax withholding are also not subject to Illinois income tax withholding.

April 21, 2008

Dear:

This is in response to the undated letter we received from Mr. Z of MEDICAL CENTER. The nature of his request and the information he provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 86 Ill. Adm. Code 1200.120(b) and (c), which may be found on the Department's web site at [www. tax.illinois.gov](http://www.tax.illinois.gov).

In his letter, Mr. Z stated the following:

We have recently discovered an error in our calculations to determine State wages for an employee of ours who is a citizen of the state of Illinois. We had been calculating their state wages without any non-taxable income, such as health insurance premiums, flexible medical spending accounts and STATE Public Employees Retirement System required deductions.

We have reviewed the Illinois Department of Revenue Withholding booklet and cannot find any information to support or disprove our current withholding calculations. Could you please send us any information you have available that may assist us in clarifying what earnings are considered taxable and non-taxable in the State of Illinois?

Response

Section 701(a) of the Illinois Income Tax Act (35 ILCS 5/701) provides:

Every employer maintaining an office or transacting business within this State and required under the provisions of the Internal Revenue Code to withhold a tax on:

(1) compensation paid in this State (as determined under Section 304 (a)(2)(B) to an individual . . .

shall deduct and withhold from such compensation for each payroll period (as defined in Section 3401 of the Internal Revenue Code) an amount equal to the amount by which such individual's compensation exceeds the proportionate part of this withholding exemption (computed as provided in Section 702) attributable to the payroll period for which such compensation is payable multiplied by a percentage equal to the percentage tax rate for individuals provided in subsection (b) of Section 201. (emphasis added)

Section 702 of the Illinois Income Tax Act (35 ILCS 5/702) allows an employee to claim exemptions based on the exemptions, subtractions from federal adjusted gross income, and credits against tax that the employee is allowed to claim on his or her Illinois income tax return.

Under the emphasized language in Section 701(a), withholding is required only from amounts that are subject to federal income tax withholding, minus the exemptions claimed under Section 702. Accordingly, payments of health insurance premiums and contributions to flexible spending accounts

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and to retirement accounts that are exempt from federal income tax and, therefore, from federal income tax withholding are not subject to Illinois withholding.

As stated above, this is a general information letter which does not constitute a statement of policy that applies, interprets or prescribes the tax laws, and it is not binding on the Department. If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b). If you have any further questions, you may contact me at (217) 782-7055.

Sincerely,

Paul S. Caselton
Deputy General Counsel – Income Tax